

Message Text

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TO AMCONSUL ST JOHNS

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E.O. 11652: N/A

TAGS: ENRG, CA

SUBJECT: U.S. PRICING POLICY ON DOMESTIC OIL

REF: ST. JOHN'S 17

1. U.S. CURRENTLY HAS TWO TIER DOMESTIC CRUDE OIL PRICING 5.35 DOLLARS/BBL. FOR "OLD" OIL FROM WELLS IN PRODUCTION AS OF DECEMBER 31, 1973 AND 11.50 DOLLARS FOR "NEW" OIL (WELLS BROUGHT ON AFTER 12/31/73) AND STRIPPER WELLS (10 BARRELS OR LESS PER DAY). OLD OIL ACCOUNTS FOR ROUGHLY 60 PERCENT OF TOTAL U.S. PRODUCTION. WEIGHTED AVERAGE PRICE OF DOMESTIC CRUDE OIL ABOUT 7.80 DOLLARS/BBL. ROUGHLY 37 PERCENT OF TOTAL U.S. CRUDE OIL IS IMPORTED AT VARIOUS PRICES. WEIGHTED AVERAGE PRICE INCLUDING IMPORTS WOULD BE AROUND 9.00-9.50 DOLLAR FIGURE CITED IN REFTEL.

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2. ENERGY POLICY AND CONSERVATION ACT (EPCA) SIGNED INTO LAW ON DECEMBER 22 HAS AS ITS PURPOSE, INTER ALIA: "TO INCREASE THE SUPPLY OF FOSSIL FUELS IN THE UNITED STATES, THROUGH PRICE INCENTIVES..." EPCA AUTHORIZES AND MANDATES PRESIDENT TO "...ESTABLISH CEILING PRICES...APPLICABLE TO ANY FIRST SALE OF CRUDE OIL PRODUCED IN THE UNITED STATES, SUCH THAT THE RESULTING ACTUAL WEIGHTED AVERAGE FIRST SALE PRICE FOR ALL SUCH CRUDE OIL...SHALL NOT EXCEED A MAXIMUM OF 7.66 DOLLARS PER BARREL." THIS "MAXIMUM WEIGHTED AVERAGE FIRST SALE PRICE" OF 7.66 DOLLARS WILL BE EFFECTIVE FOR 39 MONTHS EXCEPT AS ADJUSTED UNDER THE ACT.

3. ADJUSTMENTS TO THE MAXIMUM WEIGHTED AVERAGE FIRST SALE PRICE MAY RESULT TO TAKE ACCOUNT OF INFLATION OR AS A PRODUCTION INCENTIVE. AN ADJUSTMENT TO INDUCE GREATER PRODUCTION MAY BE MADE ONLY AFTER A FINDING BY THE PRESIDENT THAT SUCH AN ADJUSTMENT WOULD PROVIDE AN INCENTIVE FOR: (1) THE DISCOVERY OR DEVELOPMENT OF HIGH COST AND HIGH RISK PROPERTIES, (2) APPLICATION OF ENHANCED RECOVERY TECHNIQUES; OR, (3) SUSTAINING PRODUCTION FROM MARGINAL (INCLUDING STRIPPER) WELLS. SUCH ADJUSTMENTS ARE LIMITED TO THREE PERCENT PER YEAR. ADJUSTMENTS FOR INFLATION ARE LIMITED TO SEVEN PERCENT PER YEAR. TOTAL ADJUSTMENTS ARE LIMITED TO TEN PERCENT PER YEAR.

4. FEA HAS NOT ISSUED FINAL PRICING RULES UNDER THE EPCA. NOTICES ARE OUT WHICH OUTLINE FOUR METHODS TO OBTAIN THE 7.66 DOLLAR PER BARREL MAXIMUM WEIGHTED AVERAGE FIRST SALE PRICE AND PUBLIC HEARINGS HAVE BEEN HELD. THE FINAL OUTCOME COULD MAINTAIN A TWO-TIER SYSTEM SIMILAR TO THE PRESENT SETUP. EPCA DOES NOT LEGISLATE PRICE CEILINGS FOR FOREIGN CRUDE OIL. THE CEILING APPLIES ONLY TO DOMESTIC PRODUCTION.

5. TO THE EXTENT THE NEW EPCA PRICING POLICY ACHIEVES THE ACT'S PURPOSE, I.E., INCREASED DOMESTIC OUTPUT OVER TIME, HIGHER COST IMPORTED OIL WOULD BE BACKED OUT OF THE U.S. MARKET. HOWEVER, DOMESTIC CRUDE OIL PRODUCTION HAS DECLINED FOR SIX CONSECUTIVE YEARS, NATURAL GAS PRODUCTION IS FOLLOWING A SIMILAR DECLINING TREND, AND UNCLASSIFIED

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DEMAND FOR PETROLEUM PRODUCTS IS EXPECTED TO PICK UP AS THE ECONOMY REVIVES. IT WOULD APPEAR THAT IMPORTS OF PETROLEUM PRODUCTS WILL CONTINUE TO RISE IN THE SHORT AND MEDIUM TERM.

6. NEWFOUNDLAND'S COME-BY-CHANCE REFINERY, ASIDE FROM ITS OTHER DIFFICULTIES, COULD FACE PROBLEMS IF ITS COSTS ARE SUCH THAT IT CANNOT PROFITABLY COMPETE WITH U.S. REFINER-

IES UTILIZING LESS EXPENSIVE FEEDSTOCKS OR OTHER OFFSHORE
REFINERIES WITH LOWER COSTS DUE TO ECONOMIES OF SCALE,
LOCATIONAL ADVANTAGE, ETC. KISSINGER

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